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STATE PASS TO COMMERCE/ITA/MAC GAISFORD, TREASURY/JOHN HARRINGTON, AND USTR/AMERICAS OLIVER

E.O. 12958: DECL: 10/04/2029

TAGS: [ECON](#) [PREL](#) [PGOV](#) [PM](#)

SUBJECT: MARTINELLI NOT MEETING PRO-BUSINESS RHETORIC OR EXPECTATIONS

REF: A. PANAMA 711

[B.](#) PANAMA 657

[C.](#) PANAMA 756

Classified By: Ambassador Barbara J. Stephenson for reason 1.4 b and d

[11.](#) (C) Summary: The distinguishing feature of the Martinelli Administration's economic policy has been that there does not appear to be a coherent or consistent policy. It has made one major positive decision, which is to maintain sound macro economic policies. It has made one major negative decision, which is to continue to resist U.S. and OECD pressure to increase financial transparency. And it has taken a series of apparently ad hoc actions against certain business sectors which has threatened Panama's reputation as a good place to invest. Finally, widely spread rumors that Martinelli plans to appoint two cronies to the Supreme Court will further erode investment confidence and judicial independence. Martinelli campaigned on a pro-business platform and comes from the private sector, but his performance to date calls into question expectations that he will govern in a manner that provides business predictability and certainty. However, we believe that the Martinelli Administration can correct its course by embracing predictability and transparency. End Summary.

The Good

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[12.](#) (SBU) The 2010 budget for \$10,280 million, up 5.3 percent from the 2009 budget, is dominated by social services, which accounts for almost half of public spending. However, unlike many countries which have had to cut social spending or face large deficits, Panama will run only a small deficit, \$511.7 million, or 1.9 percent of the annual nominal GDP, resulting in a total public debt of 42 percent of the GNP. The continued macro economic stewardship points to the Martinelli government being able to achieve either its ambitious spending goals (such as the expected \$1 billion metro system for Panama City) or investment grade bond rating. See reftel A for more on the budget.

The Bad

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[13.](#) (C) However, the Government of Panama appears to be divided about whether and how to address demands by the OECD on tax havens and the U.S. for an effective Tax Information Exchange Agreement (TIEA). Vice President and Foreign Minister Varela told the Ambassador on October 2 that he supports constructively engaging the U.S. and OECD, but that Minister of Economy and Finance Vallarino is not yet on

board. In a separate meeting, President Martinelli told Varela to "make it happen" (referring to getting off the OECD black list), but then asked the Ambassador to weigh in with Vallarino, illustrating the division.

¶4. (SBU) As a result, and as former Vice President Al Gore put it to Minister Vallarino on September 30, Panama is worsening its reputation in global financial services by continuing to be called a tax haven. BNP Paribas announced on September 27 that it is pulling out of Panama and all other OECD black listed countries due to the increasing risk of doing business in those countries. The stubbornness of the GOP also leaves it open to abuses within the Colon Free Trade Zone, which harbors significant legitimate business but also is the route for illegitimate money and products.

¶5. (SBU) Additionally, the government's actions against US firms AES and MIT call into their commitment to maintaining a strong investment climate. AES has been hard hit by the GOP threat to unilaterally change the contracted price of water for hydroelectric generation plants owned by AES. The result of this ongoing dispute, which still has not been resolved, has been to reduce AES' bond rating in Panama to below investment grade. See reftel B for more information on AES.

¶6. (SBU) This is not the first time that the government took aim at a sector without regard to existing contracts. The GOP introduced a bill that would have eliminated contract concessions changes by reverting contracts back to their original agreement if the company harmed the people of Panama, thereby eliminating years of business predictability to contract holders. This clause appears to have been aimed at port concessions, including the US firm Manzanillo

International Terminal (MIT) which operates in Colon. The renegotiations between MIT and the GOP also have not terminated, but MIT has expressed optimism that resolution will come soon and be acceptable. The result of these two actions, plus other actions which did not directly impact American firms, has been to negatively affect business perspective on the investment climate. AES told us that plans to construct a second hydro plant in Panama valued at \$600 million have been shelved, and MIT has told us that the US owner no longer considers the Port of Colon a good place for future investment. The major change in the investment climate is that now investors are not certain that political calculations will not play a role in how contracts will be enforced; every contract could now be valid for only the five-year presidency term.

#### The (Possibly) Ugly

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¶7. (C) The increase in political interference with contractual matters is possible due to the historically weak judiciary system. In October, Martinelli will appoint two supreme court magistrates to take seats in January. The names floated do not give us optimism: Gerardo Solis, who is widely considered to be corrupt, and Jose Almengor, who is believed to be in line for a position in order to keep him from talking about Martinelli secrets. Several leading newspaper editors told the Ambassador and DCM that President Martinelli's honeymoon with the local press would end if he nominated these two to the Court. See reftel C for more information.

¶8. (C) Comment: Post will continue to monitor the Administration's activities on investment climate, financial transparency, and judicial independence. While it is clear from the actions it has taken that the Martinelli Administration has not lived up to its promises or its pedigree, post believes a nuanced message to the GOP can end certain negative trends and prevent future erosion of predictability from occurring. We are cautiously optimistic that the worst - at least regard to ad hoc actions against businesses - is over. End comment.